PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

ENERGY DIVISION **RESOLUTION G-3365**
January 12, 2006

R E S O L U T I O N

Resolution G-3365. Southern California Gas Company (SoCalGas) requests approval of 2003 shareable earnings under its Performance-Base Ratemaking (PBR) mechanism. SoCalGas' request is conditionally approved.

By Advice Letter 3386 filed on June 22, 2004
By Advice Letter 3386-A filed on April 28, 2005

SUMMARY

In Advice Letter 3386-A SoCalGas requested approval of its: 1) 2003 shareable earnings; 2) an adjustment for the actual 2003 customer count; 3) its 2003 telephone response time, customer satisfaction and employee safety performance results; and 4) the 2003 results of the Core Pricing Flexibility and Noncore Competitive Load Growth Opportunity programs.

This resolution approves SoCalGas' 2003 PBR performance results and adjustments filed with Advice Letters (AL) 3386 and 3386-A. However, the $380,000 reward for employee safety performance is approved subject to refund, and customer satisfaction and telephone response results are approved subject to later adjustment. Major elements of the resolution are summarized below.

1. There are no sharable earnings for the year 2003 because SoCalGas' rate of return (ROR) of 8.31% is 37 basis points below its authorized ROR of 8.68%.

2. SoCalGas'requested downward adjustment to the number of customer meters is approved. The adjustment to reflect 7591 fewer customer meters in 2003 results in a $2,175,049 reduction in 2003 revenue requirement.

3. SoCalGas' authorized PBR revenue requirement is increased by $179,165 to reflect the additional mobile home park master meter conversions that occurred in SoCalGas' service territory.

4. SoCalGas reports that its 2003 customer satisfaction and telephone response time results have exceeded the established targets it strives to meet under its PBR mechanism, resulting in no performance penalties. Under its authorized PBR SoCalGas does not receive any reward for telephone response time and customer satisfaction.

5. SoCalGas' Core Pricing Flexibility Program allows SoCalGas to offer optional tariffed rates and to negotiate discounted rates with its core customers. The Core Pricing Flexibility Program produced incremental revenues of $638,524, which are included in SoCalGas' net operating PBR revenues.

6. Incremental revenues associated with new noncore negotiated contracts that are part of a "California Red Team" economic development effort amounted to $274,109 in 2003.

BACKGROUND

The Commission adopted the SoCalGas PBR which was in effect during 2003 in Decision (D.) 97-07-054. This PBR established a mechanism to provide SoCalGas' management with the incentive to run its system more efficiently while providing safe, reliable service to SoCalGas' customers. D.97-07-054 required that SoCalGas file an annual advice letter by July 10th of each year summarizing the prior year's PBR performance results.

Under its PBR, SoCalGas shares revenues between ratepayers and shareholders on a progressive basis as earnings exceed the authorized rate of return (ROR) on rate base. The PBR mechanism provides for shared earnings within bands above the authorized ROR. Shareholders will retain 100% of the earnings up to 25 basis points above the benchmark ROR. Between 25 and 300 basis points above the benchmark, there are 8 bands with progressive sharing of earnings between shareholders and ratepayers. Within this range of ROR, the shareholder share of earnings rises stepwise from 25% through 100%, as the ratepayer share correspondingly declines from 75% to 0% as shown in Table 1 below. SoCalGas' ratepayers benefit from the PBR mechanism's revenue sharing scheme if SoCalGas' ROR exceeds 25 basis points above its authorized ROR. When SoCalGas' actual ROR falls below its authorized ROR, ratepayers do not share any shortfall.

Table 1
SoCalGas PBR Revenue Sharing Bands

Bands	Shareholder %	Ratepayer %
Actual ROR below authorized - no sharing		
Actual ROR 0-to 25 basis points above authorized – no sharing	100%	00%
25-50	25%	75%
50-75	35%	65%
75-100	45%	55%
100-125	55%	45%
125-150	65%	35%
150-200	75%	25%
200-250	85%	15%
250-300	95%	05%
300-above	100%	00%

SoCalGas' 2003 authorized rate of return was updated to 8.68% in AL 3199-A in accordance with the PBR market indexed capital adjustment mechanism (MICAM) formula.

SoCalGas' PBR mechanism also incorporates performance standards associated with SoCalGas' customer satisfaction, service quality, and employee safety performance, along with financial incentives to meet these performance standards.

Additionally, D. 97-07-054 required SoCalGas to adjust its natural gas revenue requirements annually in years subsequent to 1997 using an established PBR indexing formula that is applied to the revenue requirement per customer.

SoCalGas filed AL 3386-A on April 28, 2005 to correct its safety incentive reward.

SoCalGas found through further review that its incident rate was 6.4 incidents per 200,000 hours worked compared to the 6.0 incidents per 200,000 hours worked that was previously calculated and reported in AL 3386. The change in incident rate is primarily the result of including OSHA recordable incidents recorded in 2004 that actually occurred in 2003. Based on the revised incident rate the reward was recalculated to be $380,000, $80,000 less than that reported in AL 3386.

Southern California Edison Employee Misconduct Under Investigation

Southern California Edison Company (Edison) also operated under a base rate PBR, approved by the Commission in D.96-09-092. Like the SoCalGas and San Diego Gas & Electric Company (SDG&E) PBRs, the Edison PBR included quality of service incentives. The Edison quality of service incentives were related to customer satisfaction, employee health and safety, and electric reliability.

The Commission's Consumer Protection and Safety Division (CPSD) is conducting its own investigation of Edison's reporting of its PBR incentive data.

The investigation is not concluded yet.

In Resolution E-3871 the Commission approved SDG&E's 2003 PBR rewards subject to refund.

NOTICE

Notices of ALs 3386 and 3386-A were made by publication in the Commission's Daily Calendar. SoCalGas states that a copy of these Advice Letters was mailed and distributed in accordance with Section III-G of General Order 96-A.

PROTESTS

No protest to Advice Letter 3386 or 3386-A was received.

DISCUSSION

Revenue sharing

The Commission has reviewed SoCalGas' results of operations and revenue sharing calculations for 2003, and concurs that no revenue sharing results from SoCalGas' 2003 financial performance.

SoCalGas' revenue sharing scheme allocates Net Operating Income (NOI) that exceeds its authorized return between shareholders and ratepayers according to a set of sharing tiers that awards shareholders with an increasing portion of the earnings as the actual ROR increases above the authorized ROR. SoCalGas' shareholders are at risk for all of the recorded NOI associated with an actual ROR that is below the authorized ROR.

SoCalGas' actual ROR of 8.31% is 37 basis points below its authorized ROR of 8.68%. SoCalGas' ROR of 8.68% was established in AL 3199-A, in accordance with the Market Indexed Capital Adjustment Mechanism (MICAM) formula. Thus, there is no income to be shared between shareholders and ratepayers for 2003.

SoCalGas' Customer Count Adjustment Reduces its Revenue Reqirement.

Under SoCalGas' PBR in effect in 2003, SoCalGas multiplied its forecasted customer count by the revenue requirement per customer that results from the PBR indexing formula in order to update its revenue requirement at the beginning of each year. This revenue requirement is later adjusted based on the actual number of customers that received service from SoCalGas.

With AL 3193, filed on October 1, 2002, SoCalGas forecasted that it would provide natural gas to 5,200,449 customers in 2003. With AL 3386 and 3386-A, SoCalGas updated the actual number of customers it provided service to in 2003, based on the average recorded number of active meters in SoCalGas' service territory in 2002. The adjusted actual active meters for 2003 were 5,192,858, or 7,591 fewer than forecast. At the 2003 base margin per customer of $286.53 SoCalGas' proposed revenue requirement should be reduced by $2,175,049 as a result of its customer count adjustment.

SoCalGas Earned a Mobile Master Meter Conversion Allowance

Assembly Bill (AB) 622 permitted the transfer of a mobile home park's master meter operational responsibilities from the owner of the mobile home park to the natural gas company whose service territory encompasses the mobile home park. A total of 969 meters were added to SoCalGas' system as a result of AB 622. Additional SoCalGas meters established under AB 622 increased the authorized revenue requirement.

In 2003, there were 70 net new individual meters from AB 622-mandated SoCalGas takeover of converted mobile home park facilities. These 70 meters are not included in the customer count above and must be added to the 969 meters from conversion through 2002 to total 1,039 conversions. The authorized effective avoided cost for sub-metered credit is $172.44 per year per meter. The calculated avoided cost for 1,039 meters is $179,165.

SoCalGas Customer Satisfaction and Telephone Response Time Performance Was Adequate to Avoid a Penalty

SoCalGas' PBR mechanism includes performance targets for customer satisfaction based on SoCalGas' average performance in 1994 through 1996.

These performance targets are associated with customer satisfaction survey results pertaining to SoCalGas' telephone service representatives, appointment scheduling practices, field service representatives, and on-time arrival for service representatives. Performance results are gathered from customers that respond to a telephone survey.

Under the PBR mechanism SoCalGas can be penalized for failure to meet customer satisfaction and service quality targets. SoCalGas is penalized $10,000 for each 0.1 percentage point its performance falls below the dead band associated with these targets. In 2003, SoCalGas' performance exceeded its targets in all four service areas. Since SoCalGas exceeded its customer satisfaction target, SoCalGas should not be penalized.

SoCalGas' PBR mechanism also includes a telephone response time performance standard, which requires 80% of regular calls to be answered within 60 seconds, and 90% of emergency calls to be answered within 20 seconds. SoCalGas is assessed a $20,000 penalty for each 0.1 percent decline in performance below each performance standard.

SoCalGas reports that in 2003 it was able to answer 83.2% of all regular telephone calls in less than 60 seconds and 92.7% in less than 20 seconds.

SoCalGas' 2003 telephone response rate performance does not result in penalties being assessed on its shareholders.

Under the adopted PBR, SoCalGas is assessed a penalty for failing to meet customer satisfaction and telephone response time targets, but cannot earn a reward under its PBR.

SoCalGas Earned a $ 380,000 Reward for Employee Safety

SoCalGas' PBR includes an incentive for employee safety, and allows a reward if the Company's performance is better than the benchmark. SoCalGas' annual employee safety benchmark is set at an Occupational Safety and Health Administration (OSHA) frequency of 9.3 incidents per 200,000 (100 employees at 2,000 hours/year) hours worked with a dead band of plus or minus 1.0. For each tenth of a point SoCalGas scores above or below the dead band, it is penalized/rewarded $20,000.

The SoCalGas OSHA frequency standard is calculated by multiplying the actual number of annual, recordable, injuries by 200,000 (100 employees at 2,000 hours/year) and dividing this figure by the total number of OSHA working hours. As corrected by SoCalGas AL 3386-A, SoCalGas' performance resulted in an OSHA frequency of 6.4 and a reward of $380,000 in 2003.

SoCalGas calculated its safety performance rewards correctly.

Core Pricing Flexibility Adjustment Produced Incremental Revenues

Under the Core Pricing Flexibility Program, authorized by D.97-07-054 and D.98-01-040, SoCalGas may offer optional tariff rates and negotiate discounted tariff rates with new or existing core customers for the purpose of load growth and load retention.

The Commission authorized a Core Fixed Cost Account (CFCA) adjustment mechanism in order to protect core customers from the risk of revenue shortfalls associated with optional tariff rates and negotiated discounted tariff rates. This adjustment mechanism calculates revenues that represent base revenues that should have been credited to the CFCA in the absence of optional or negotiated tariff rates.

SoCalGas' Core Pricing Flexibility Program produced incremental revenues of $638,524 that are included in its net PBR operating revenues. We find these incremental revenues to be reasonable.

Noncore Competitive Load Growth Opportunities Produced Incremental Revenue

D.00-04-060 authorizes SoCalGas' revenue treatment for new negotiated contracts that are part of an economic development effort and contracts where Rule 38[1] shareholder funding has been used. Under this arrangement, SoCalGas shareholders are responsible for any reduction in noncore revenues that may occur due to discounting, while revenue gains will be shared between ratepayers and shareholders in accordance with the PBR sharing mechanism. These contracts produced incremental revenues of $274,109 in 2003 that are included in SoCalGas' net PBR operating revenues. Since there is no revenue sharing there is no distribution to ratepayers and shareholders.

Employee safety PBR reward of $380, 000 is subject to refund, and customer satisfaction and telephone response time results are subject to adjustment.

At this time, the Commission has no information that SoCalGas' employees or management participated in misconduct in relation to its PBR data collection or in the reporting of its results, and we have no reason to believe that its employee safety PBR reward is not accurate and honestly earned.

Upon learning of reports of Edison misconduct, in 2004 SoCalGas conducted its own internal review of its procedures and data reporting related to its safety indicators. SoCalGas found no evidence of manipulation of its safety performance indicator. SoCalGas did discover an error in reporting instances of safety events, and submitted AL 3386-A to correct the error which resulted in a small revision to its performance penalty.

Nevertheless, we can not ignore the information we have received to date from Edison related to its PBR. The Commission approved significant PBR rewards to Edison for years, amounting to tens of millions of dollars, before the Commission became aware of the widespread misconduct that was apparently occurring, among both staff level employees and supervisors.

[1] Rule 38 is aimed at stimulating customer interest in new, high efficiency gas fired equipment.

Our CPSD staff is continuing to investigate Edison's misconduct, and have yet to issue their findings. If CPSD's investigation concludes that an independent investigation of the service quality incentives of other utilities including SoCalGas is warranted, we will preserve the authority to recover the employee safety reward approved herein today. Similarly, service quality results in areas of customer satisfaction and telephone response time results are subject to adjustment and refund should the results of a SoCalGas investigation reveal that such rewards were improperly paid out to SoCalGas.

In Resolution E-3871 the Commission similarly approved SDG&E's reward subject to refund based on the outcome of the CPSD's investigation of the Southern California Edison's procedures for gathering PBR data. Therefore, the employee safety reward and other service quality results we approve in this resolution should be subject to refund in the event that a future SoCalGas investigation determines such the reward was ill gotten or the results were incorrectly reported.

Effective Date

In AL 3386 SoCalGas requested an effective date of August 1, 2004. In AL 3386-A SoCalGas requested an effective date of June 30, 2005. We held AL 3386-A pending the outcome of Edison's investigation. We will now approve AL 3386-A effective today.

COMMENTS

Public Utilities Code section 311(g)(1) provides that this resolution must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission. Section 311(g)(2) provides that this 30-day period may be reduced or waived upon the stipulation of all parties in the proceeding.

All parties in the proceeding have stipulated to waive the 30-day waiting period required by PU Code 311 (g) (1) and the opportunity to file comments on the draft resolution. Accordingly, this matter will be placed on the Commission's agenda directly for prompt action.

FINDINGS

1. SoCalGas filed Advice Letter 3386 on June 22, 2004 to request approval of its 2003 PBR shareable earnings report.

2. SoCalGas filed Advice Letter 3386-A on April 28, 2005 to correct the safety incentive reward reported in Advice Letter 3386.

3. There were no protests against AL 3386 or 3386-A.

4. SoCalGas' actual ROR of 8.31% is less than its authorized ROR by 37 basis points; therefore there is no revenue sharing.

5. The average recorded number of active meters in SoCalGas' service territory in 2003 was 5,192,858 or 7,591 less than forecast which results in a reduction in revenue requirement by $2,175,049 as a result of its customer count adjustment.

6. In 2003, SoCalGas gained 70 gas meters as a result of taking over the operational responsibilities of mobile home parks' master meters and 969 gas meters from conversions through 2002. SoCalGas' authorized PBR revenue requirement was increased by $179,165 due to mobile home park meter conversions.

7. In 2003, SoCalGas' customer satisfaction and telephone response rate performance exceeded the benchmarks. As a result, no penalties should be assessed for these performance indicators.

8. SoCalGas' performance resulted in an OSHA frequency of 6.4 and a reward of $380,000 in 2003.

9. SoCalGas' Core Pricing Flexibility Program produced incremental revenues of $638,524 in 2003 that SoCalGas has included in SoCalGas' net PBR operating revenues.

10. SoCalGas' Noncore Competitive Load Growth Opportunities Program produced additional revenues in 2003 of $274,109 that SoCalGas included in PBR operating revenues.

11. SoCalGas AL 3386-A should be approved with an effective date of today.

12. The $380,000 employee safety reward is subject to refund. Similarly, service quality results in areas of customer satisfaction and telephone response time results are subject to adjustment and refund in the event that the current investigation by the Commission's Consumer Protection and Safety Division (CPSD) concludes that a broader investigation of service quality incentives including those under SoCalGas' PBR is warranted.

THEREFORE IT IS ORDERED THAT:

1. SoCalGas' Advice Letter 3386-A is approved with modifications.

2. The employee safety reward is approved subject to refund. Customer satisfaction and telephone response time results are subject to adjustment and refund in the event that the current investigation of Edison's PBR results by the Commission's Consumer Protection and Safety Division (CPSD) concludes that a broader investigation of service quality incentives including those under SoCalGas' PBR is warranted.

This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on January 12, 2006; the following Commissioners voting favorably thereon:

____
STEVE LARSON
Executive Director

MICHAEL R. PEEVEY
PRESIDENT
GEOFFREY F. BROWN
DIAN M. GRUENEICH
JOHN A. BOHN
RACHELLE B. CHONG
Commissioners